United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

77-7230

United States Court of Appeals

FOR THE SECOND CIRCUIT

FILED
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SECOND CIRCUIT

Docket No. 77-7230

WILLIAM J. SOLLOWAY,
Plaintiff-Appellant,

—against—

THE FIRST INDIANA CORPORATION, CAN-WEST 1972 GAS PARTNERSHIP, a limited partnership and CAN-WEST 1973 GAS PARTNERSHIP, a limited partnership,
Defendants-Appellees.

APPEAL FROM ORDER OF UNITED STATES DISTRICT COURT REFUSING PLAINTIFF'S MOTION TO REOPEN JUDGMENT

BRIEF FOR APPELLANT

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UNITED STATES COURT OF APPEALS
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WILLIAM J. SOLLOWAY,

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- against - Docket No. 77-7230

THE FIRST INDIANA CORPORATION,
CAN-WEST 1972 GAS PARTNERSHIP,
a limited partnership, and
CAN-WEST 1973 GAS PARTNERSHIP,
a limited partnership,

Defendants-Appellees,

----------X

BRIEF OF PLAINTIFF-APPELLANT

ISSUE PRESENTED FOR REVIEW

Plaintiff entered into a stipulation of settlement and permitted an order of dismissal to be entered. Plaintiff would not have entered into the settlement, but for certain statements made by the defendants' agent that indicated that the defendants were nearly insolvent and could not provide anything more in settlement without throwing defendants into bankruptcy. Plaintiff asked for financial support for these claims, and was told that it would be forthcoming. When they were finally produced months later, they indicated that the claims of defendants were untrue, and that defendants were in good shape financially. Plaintiff also would not have entered into the stipulation but for the fact that the court included a "reopening provision" which provided for reopening for "good

cause". Given these facts, should the Court have permitted reopening?

STATEMENT OF THE CASE

This is an appeal from an Order of Judge Robert Ward denying a motion of the plaintiff, WILLIAM J. SOLLOWAY, to re-open an action that had been dismissed by Order of Dismissal signed by Judge Ward on April 8th, 1976. Plaintiff seeks to have this matter returned to the trial calendar according to the "re-opening" provision in the Order.

The Motion was made by Notice of Motion dated August 27th, 1976 (A-25). Judge Ward, in an opinion and order, dated October 14th, 1976 (A-38) referred the matter to United States Magistrate Harold J. Raby to hear and recommend whether plaintiff's motion should be granted. A hearing was held before Magistrate Raby on February 9th, 1977. Magistrate Raby issued a report (A-55) dated March 11, 1977, recommending that the plaintiff's motion be denied.

Thereafter, plaintiff SOLLOWAY filed a Notice of Objection to the report of the United States Magistrate (A-57), which also requested a de novo determination of the facts by Judge Ward.

Judge Ward, on April 11, 1977, overruled plaintiff's objections to the report of Magistrate Raby, and adopted the recommendations, confirmed the report, and refused to re-open the case. (A-62).

Plaintiff SOLLOWAY in this appeal, seeks to reverse Judge Ward's

decision and thereby restore this case to the trial calendar so that the plaintiff can have his day in court.

RELEVANT FACTS

Plaintiff, WILLIAM J. SOLLOWAY, is a Canadian citizen. He has extensive legal and financial experience in all facets of the oil and gas business. Particularly applicable in this case, plaintiff has extensive Canadian contacts, technical background and experience to introduce Canadian oil and gas companies to the American financial community, construct and originate feasible proposals to finance oil and gas development drilling and production, and, finally, to fashion such financing into limited partnerships saleable to selected investors seeking "tax shelter" investments, thus providing the necessary "off balance sheet" financing to Canadian exploration companies to develop their mineral leases with United States "tax" dollars. The United States tax advantage of deducting drilling expenses from ordinary income of a taxpayer has no counterpart in the Canadian Income Tax Act for Canadians, and therefore Canadian exploration companies seek American financing.

Plaintiff, as a member of the Canadian Bar for 19 years, has valuable experience and status in developing energy related tax shelters.

In 1971, plaintiff met WILLIAM HAEBERLE, a professor of Business Administration at the University of Indiana, and formerly an associate of the New York Stock Exchange firm of BLAIR & Co., until he

consented to an SEC injunction for (a) violations of the anti-fraud provisions of Federal Securities laws and b) selling securities without proper disclosure and making misleading representations to purchasers. Plaintiff, unaware of Haeberle's SEC injunction, together with Haeberle established the defendant, FIRST INDIANA CORPORATION ("FINCAP") as a vehicle for originating and marketing oil and gas tax shelters. FINCAP was incorporated in Delaware in 1972. Haeberle was elected President and Chairman of the Board and Chief Executive officer and plaintiff Solloway became Senior Vice President and a Director. Both Plaintiff Solloway and Haeberle were stockholders.

Thereafter FINCAP organized oil and gas drilling tax shelter partnerships with a Canadian oil exploration company introduced by the plaintiff. Limited partnership units were offered to a number of wealthy investors in 1972 and 1973. At issue in the case at bar, are the CAN-WEST 1972 GAS PARTNERSHIP and CAN-WEST 1973 GAS PARTNERSHIP. the co-defendants, who raised $725,000 to drill for natural gas.

Eventually, after the money raising activities and the closing of the 1973 Gas Partnership, a dispute arose and the plaintiff was "fired" by Haeberle. From 1973 to the time of the pre trial conference before Judge Ward on April 1976, plaintiff received no partnership financials nor engineering evaluation reports of the two partnerships proven gas reserves, nor were

there any FINCAP shareholders meetings since April, 1974 to inform the plaintiff of any progress that was being made. Therefore, still unresolved were issues of monies SOLLOWAY claimed were due him, including certain Finder's fees, out of pocket travel expenses, back salary, shares of FINCAP stock, participations in oil and gas revenues earned by the partnerships, and compensation for certain income the plaintiff contributed to FINCAP. To resolve these debts, the plaintiff instituted this action.

The case came before Judge Ward on April 8, 1976. The parties negotiated without financials from 10:00 a.m. to 6:00 p.m. The result was a stipulation of settlement (A-20) and Judge Ward's Order of Dismissal (A-19).

The Order of Dismissal stated that "this action is hereby dismissed with prejudice and without costs, but without prejudice to the right, upon good cause shown, within 30 days, to reopen the action if settlement is not consummated". There were a number of extensions to the 30 day limit owing to the defendants failure to produce financials and engineering reports and finally, plaintiff made a formal motion (A-25) to reopen in order to have his day in court.

The settlement was never consummated, and the plaintiff SOLLOWAY insists that by the terms of the Order of Dismissal, this case should be reopened. Plaintiff SOLLOWAY pleads that he was misled into making the settlement and believed the settlement to be contingent upon all the defendants financials and engineering reports supporting the defendants' many representa-

tions. The entire settlement and proposed security agreement were premised on the defendants' representations, unsupported by any financials or proven gas engineering reserves, that the two CAN-WEST GAS PARTNERSHIPS were a failure and further, that any settlement greater than the settlement proposed, would throw the defendants into bankruptcy and also that the defendants needed five years in order to pay the settlement payment of $30,000.00. It was most unusual that the defendants appeared at the settlement conference to take that position without any financial information whatsoever or engineering reports which were freshly in their possession to support its contentions. The terms of the settlement were that the plaintiff was to receive $30,000.00 payable over a five year term and approximately 1% of the Partnership cashflow and he surrendered rights to 10,000 shares of FINCAP stock, a cash claim of $55,903., and a contractual right to approximately 3% of the Partnership income.

Eventually, the defendants produced partial financials and a current engineering report which had been in the defendant's possession at the time of the settlement. From these documents, a far different financial picture emerged. Defendants have a proven present and future cash flow of $10,878,000.00 of which $1,956,000.00 has and will be paid by 1980 (the time period fot the payment of the $30,000.00) and the stock rights have great value. The proposed settlement was based on inaccurate and non supportable contentions furnished by the defendants which makes the settlement markedly inequitable

and it is respectfully urged that the matter be restored to the calendar.

It is SOLLOWAY's contention that he only entered into the settlement because of 1.) the false representations of the defendants; 2.) the assurance that the Order of Dismissal would include a "30 day reopening provision" if the financial proof did not support the defendant's settlement statements. As to the latter, it is clear that the language and intent of the Court and the parties suggests that if there has indeed been a showing of good cause sufficient to warrant reopening, the refusal of the Court below to permit reopening contradicts its own Order of Dismissal.

POINT I

MAGISTRATE RABY MADE ERRORS OF FACT AND LAW IN HIS DETERMINATION

At the hearing before Magistrate Raby, plaintiff SOLLOWAY presented certain exhibits that indicated clearly that at the time of the settlement conference before Judge Ward, the defendants had financial information, which they did not reveal to the plaintiff, which indicated that the defendants were not in dire financial straits. (Plaintiff SOLLOWAY insists that as he believed it, the defendants would back up their claims by financial data as soon as it was available, and should that information be at variance with the claims made in the settlement conference, he could simply

invoke the "reopening provision" to get the case back on the trial calendar. Thus, both the actions of the defendants and the Court bore heavily on the plaintiff to make the decision to accept at that time a settlement he would not have otherwise entered into.)

At the hearing before Magistrate Raby, plaintiff put into evidence three exhibits. Scrutiny of these indicates that the defendants were in financially good shape. Moreover, they contain evidence known and prepared prior to the date of the settlement conference.

One exhibit, the D & S Petroleum Consultants' Evaluation Report of April 1, 1976 (the settlement conference was April 8, 1976) clearly states that gas sales of the defendants 1972 and 1973 CAN-WEST PARTNERSHIPS will amount to $10,878,000.00, (A-78) at projected prices which have now increased so that future income may be estimated at $13,000,000.00. Plaintiff's contractual agreement, the basis of the lawsuit, equates to roughly 3% of all income to plaintiff, or approximately $400,000.00. Hence, it is clear that the plaintiff would have never settled for a mere $30,000.00 unless he was misled as to the value of the defendants, and told that, if the claims of the defendant were not true, he could reopen the case.

It is also clear that FINCAP's insistence that it would need five years to pay out the $30,000.00 settlement was misleading both the plaintiff and the Court. The evaluation report (A-77)

indicates the proven gas incomes for the Partnerships to be:

1976	Income was	$51,000.00
1977	Income is	82,000.00
1978	Income to be	528,000.00
1979	Income to be	661,000.00
1980	Income to be	634,000.00
FIVE YEAR TOTAL:		$1,956,000.00

It is clear that Magistrate Raby was not aware of these figures, which were in evidence and which Plaintiff tried to explain. Magistrate Raby made his determination immediately at the hearing without looking at these books and reports.

This overlooking of crucial factual matter is error sufficient to warrant reversal of the determination of the Magistrate.

POINT II

THE ORDER OF JUDGE WARD REFERRING THE MATTER TO MAGISTRATE RABY GAVE INCORRECT INSTRUCTIONS AS TO THE FACTORS TO BE CONSIDERED.

The o der of Judge Ward (A-48) that refers the matter to the Magistrate was incorrect for several reasons:

1. It was at variance with the Order of Dismissal. The Order of Dismissal (A-19) was very specific as to the grounds for which reopening would be permitted. The Order of Dismissal was one of the reasons why plaintiff SOLLOWAY even entered into the settlement stipulation. By the terms of the Order of Dismissal, the only necessary showing to reopen was

"good cause shown". In fact, plaintiff SOLLOWAY had been led to believe that the settlement could be routinely opened upon good cause. However, upon hearing the motion, Judge Ward referred the matter to Magistrate Raby in a seven page decision (A-38). Rather than instructing Magistrate Raby to determine whether there was "good cause shown", Judge Ward instructed Magistrate Raby to look for "misrepresentations" (A-43). This is a much more difficult showing, and it was not even suggested in the Order of Dismissal. Hence, Judge Ward was, after the fact,changing the very terms of the settlement in making the requirement to reopen much more difficult to meet. Secondly, the instructions to Magistrate Raby looked only to fraud. It did not instruct Magistrate Raby to consider other grounds that would also justify the reopening. Magistrate Raby was not instructed to look for any other "good cause shown" to reopen. Specifically, Magistrate Raby was not instructed to decide if there were grounds under Rule 60B, Federal Rules of Civil Procedure, which include, in addition to fraud and misrepresentation, "other misconduct of an adverse party" or "any other reason justifying relief". Hence, even if Magistrate Raby's findings on fraud were correct, there was and has been no holding as to whether other grounds were met.

POINT III

AS REQUIRED BY THE COURT'S ORDER OF DISMISSAL, PLAINTIFF HAS SHOWN JUST CAUSE FOR REOPENING THIS CASE

The situation that has arisen is specifically the type of situation that a "Reopening Provision" is intended to cover.

The Court Order reads as follows:

> "The court having been advised by counsel for the parties that the above action, that is this action, has been settled it is ordered that this action is hereby dismissed with prejudice and without costs but without prejudice to the right upon good cause shown within 30 days to reopen the action if settlement is not consummated."

In the interest of Court efficiency, settlements are always desirable. However, a party often necessarily makes his concessions based on the work of his adversary, rather than on facts proven at trial. Hence, a settlement can be worked out in which all sides and the Court recognize that some "loose ends" remain to be resolved. But it is possible that a party can prevent, by design or otherwise, the consummation of the settlement. Hence, the "Reopening Provision" is invaluable as a tool for encouraging settlement. Without it, parties would be far more reluctant to agree on a settlement for fear that they would be bound fully by a settlement that was never fully consummated.

The Order of the Court stands on its own and is independent and in addition to the settlement stipulation. Regardless of the grounds for reopening decided upon in the settlement

stipulation, the Court has provided for reopening upon showing of good cause. Plaintiff has shown good cause. Based on representations made to Judge Ward and to the plaintiff that the defendant was nearly insolvent, plaintiff agreed on a settlement with a five year payout that he never would have accepted had the true picture of defendants been available.

Conerly v. Flower, 410 F. 2d. 941 (8th Cir., 1969), upheld a District Court's vacating of a consent judgment on the grounds of fraud. The defendant, in a personal injury case, represented that his maximum insurance coverage was $20,000., and plaintiff agreed to settle within that limit. When it later appeared that the defendant had more than that amount of insurance, the court vacated the settlement. This is, of course, similar to the case at bar, where the defendants represented that there was a maximum amount they could pay out in settlement or else they would be driven into bankruptcy.

Plaintiff argues that the defendants misled not only the plaintiff, but also committed a fraud upon the Court. Particularly blatant was the insistence by defendants that its economic situation dictated a payout of the $30,000. settlement over five years. This claim of defendants is ludicrous in light of the fact that proven gas well income from 1976 to 1980 is $1,956,000.00 (see A78-A-80), according to the April 1, 1976 engineering report on proven gas production.

POINT IV

EVEN IN THE ABSENCE OF A "REOPENING PROVISION", RULE 60B OF THE FEDERAL RULES OF CIVIL PROCEDURES AUTHORIZES REOPENING IN THIS CASE.

Even if there had not been a reopening provision in the judgment, Rule 60-b provides that a Court may relieve a party from a final judgment in a number of instances.

Rule 60-b provides, in pertinent part:

> "Mistakes; Inadvertence; Excusable Neglect; Newly Discovered Evidence; Fraud, etc. On motion and upon such terms as are just, the court may relieve a party of his legal representative from a final judgment, order or proceeding, for the following reasons: (1) mistake, inadvertence, surprise, or excusable neglect; (2) newly discovered evidence which by due diligence could not have been discovered in time to move for a new trial under Rule 59(b); (3)...misrepresentation, or other misconduct of an adverse party;... (6) any other reason justifying relief from the operation of the judgment. The motion shall be made within a reasonable time....."

Rule 60-B was intended to be flexible. "Courts should and do give liberal construction to 60(b)," 2 Moore's Federal Practice, §60.18(8).

Plaintiff's moving affidavit (A-27) establishes facts that would justify granting the motion under subdivisions 1, 2, 3 or 6, supra.

During a day of intense settlement negotiations, plaintiff was assured that later information would confirm representations made that day. In fact, much of the information was never turned over; what was turned over indicates that the defendant's

representations were at variance with the facts.

In Petry v. General Motors, 62 FRD 357 (U.S.D.C., ED,Pa, 1974), the Court found that where plaintiff relied on defendant's answers to interrogatories as the basis for entering into a stipulation of settlement, and it was shown that the answers were false, that this was "fraud, misrepresentation, or misconduct" within the meaning of Rule 60(b)(3). In the same way, in the case at Bar, plaintiff entered into the settlement, relying on statements of the defendant that defendant knew to be false when they were made.

In U.S. v. Jordan, 6 Cir, 186 F 2d 803, affirmed 342 US 911, 7255 ct. 305, 96 L Ed. 682, in an eminent domain case, a judgment was entered based upon stipulations of settlement. When it was later shown that at the time of the stipulation the parties did not have information concerning damage to the property in question, the District Court set the settlement aside. On appeal, the Sixth Circuit said that,

> "the releases and stipulations, together with the judgments entered on the stipulations, were properly set aside as being based on a mutual mistake of fact."
> U.S. v. Jordan, id, at page 807.

Plaintiff's discovery since the date of the settlement that the facts are other than represented is newly discovered evidence sufficient to warrant reopening under subdivision 2.

If what occurred was not a mutual mistake of fact, it would appear that the Defendant knew his representations were at

variance with reality. This would amount to misrepresentation, clearly strong grounds for reopening.

Furthermore, Mr. SOLLOWAY's affidavit (A-) establishes subsequent refusal to provide financial information, which is contrary to the terms of the Agreement. This is certainly "other misconduct" by the adverse party.

In L. M. Leathers' Sons v. Goldman, (CA 6th, 1958) 252 F2d 188, there was a consent judgment in a patent case. The judgment was obtained by a promise that Plaintiff would grant a license to the adverse party. The plaintiff subsequently refused to comply with its part of the contract. The Court held, at page 190:

> "The refusal on the part of the appellant to carry out its part of the contract by which the judgment was obtained fully justified the Court in taking appropriate action to restore the parties to their status quo prior to the execution of the Agreement."

In addition to there being cause for reopening based on subdivisions 1, 2 or 3, this is also a case for the operation of subdivision 6, "Any other reason justifying relief from the operation of the judgment."

The leading case or Rule 60-B is Klapport v. United States, (1949) 335 US 601, 336 U.S. 942, 69S.Ct. 384, 93 L.ed.266, 1099.

Speaking of subdivision (6), Mr. Justice Black stated:

> "In simple English, the language of the 'other reason' clause, for all reasons except the five particularly specified, vests power in Courts adequate to enable them to vacate judgments whenever such action is appropriate to accomplish justice."

Kelly v. Greer, 334 F2d 434, involved an order of dismissal similar to that in the instant case. The court order dismissed with prejudice where the settlement stipulation provided that the details of the settlement would be worked out before a certain date. The plaintiff subsequently moved for restoration. The Third Circuit ruled that the District Court had jurisdiction to do so "in the interests of Justices (id at P. 437).

Aro Corp. v. Allied Witan Company, 65 F.R.D. 513 (1975) (U.S.D.C., N.D. Ohio, 1975) involved a case where the parties entered into a stipulation of settlement. When the defendants failed to comply with the express terms of the agreement, the plaintiff moved to reopen and restore the case to the calendar. The Court agreed, and ordered the case back on the trial cale r.

CONCLUSION

For all of the foregoing reasons, it is urged that the Court reconsider the determination of Judge Ward, order the matter restored to the trial calendar and plaintiff be given his day in Court.

September 17, 1977

Respectfully Submitted,

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Plaintiff-Appellant,
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AFFIDAVIT OF SERVICE BY MAIL

Docket No. 77-7230

State of New York

County of Kings

ALBERT SENSALE, being duly sworn, deposes and says, that deponent is not a party to the action, is over 18 years of age and resides at 914 BROOKLYN AVE BROOKLYN N Y

That on the 22nd day of SEPTEMBER, 1977, deponent served the within BRIEF & APPENDIX upon DONOVAN, LEISURE, NEWTON & IRVINE 30 ROCKEFELLER PLAZA New York, New York 10020

Attorney(s) for the APPELLEES in the action, the address designated by said attorney(s) for the purpose by depositing a true copy of same enclosed in a postpaid properly addressed wrapper, in a post office official depository under the exclusive care and custody of the United States Post Office department within the State of New York.

Albert Sensale

Sworn to before me,

This 22nd day of SEPTEMBER 1977

Pierre L. St. Phard

PIERRE L. ST. PHARD
Notary Public, State of New York
No. 24-4504294
Qualified in Kings County
Commission Expires March 30, 1979